

# **“Adjusted NYMEX Settle”**

## **Calculation**

- **NYMEX Time Factor Differential (“TFD”)**  
determined every trading day while the  
delivery month is prompt month on NYMEX
- **Daily TFD’s averaged together to determine  
appropriate average TFD**
  - Average TFD determined prior to delivery month
- **Actual delivery price is average of NYMEX  
Prompt settle during delivery month, plus or  
minus average TFD**



— CONSULT THE FRONTIERS OF FREEDOM —

# Time Factor Differential Formula

$$\text{TFD} = \text{MTM}_{(1-2)} \times \text{A/D} + \text{MTM}_{(1-3)} \times \text{B/D}$$

Where:

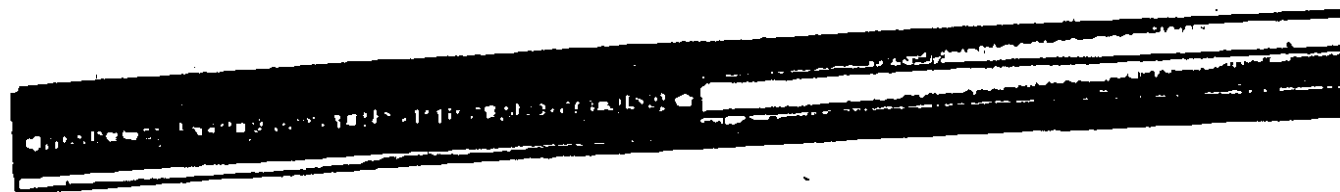
$\text{MTM}_{(1-2)}$  = NYMEX settle price for Prompt month, minus settle price for 2nd month on strip

$\text{MTM}_{(1-3)}$  = NYMEX settle price for Prompt month, minus settle price for 3rd month on strip

A. = Number of days in delivery month when Prompt month traded on NYMEX is the first calendar month following trading month

B. = Number of days in delivery month when Prompt month traded on NYMEX is the second calendar month following trading month

D. = Number of days in delivery month



# Example of Time Factor Differential Calculation

**Performed on September 3, 1996 for October 1996 Deliveries**

**NYMEX Settle Prices on September 3, 1996:**

**Oct 96: \$23.40, Nov 96: \$22.66, Dec 1996: \$22.05**

**During October delivery month, November will trade as prompt through October 22, then December will trade as prompt. October has 31 days.**

$$\text{TFD} = (23.40 - 22.66)(22/31) + (23.40 - 22.05)(9/31) = \$0.917/\text{BBL}$$

**This means that a party selling October crude oil based on the NYMEX settle prices during the month of October could receive \$0.917/BBL over the average of the NYMEX prompt settle prices during October, including weekends and holidays in the average at the same NYMEX value as the previous trading day.**



**Summit Energy Services, Inc. 10000 West 10th Avenue, Suite 100, Denver, CO 80202**

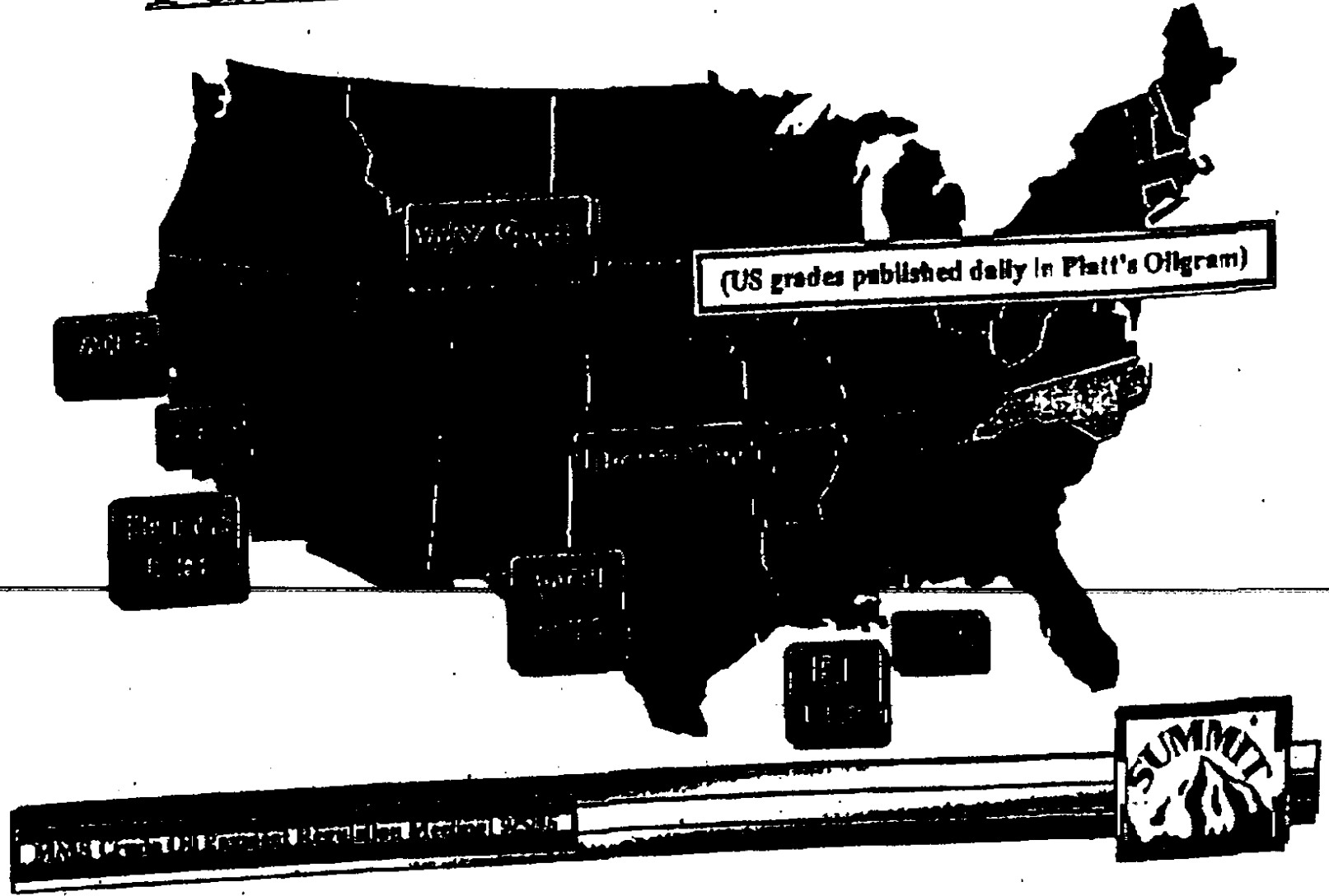
# **Market Average Price Basis**

## **Recommendation (cont.)**

- Use Platt's Oilgram differentials for grade trade differentials between Cushing and major market centers
  - Using average of trading days while delivery month is prompt on cash market
    - From 26th day of two months prior to delivery, through 25th day of one month prior to delivery
  - Platt's is not perfect, but currently best reflects actual market values
    - Recognize potential to evolve/improve



# US Grade Trading Locations Published in Platt's Oilgram



# **Market Average Exchange Differential** **Establishment Procedure**

- Payors report actual exchange terms
- MMS calculates and publishes market average every 6 months
  - Based on common aggregation points to public spot market centers
  - MMS establishes market differentials in areas where no reported data is available
    - Extrapolating from known areas
- Payors can challenge MMS differentials



# **Procedure for Challenging MMS Market Average Exchange Differential**

- **Burden of proof on challenger to show that MMS differential is not reasonable**
  - (If a party has actual exchange values, then it is supposed to pay based on those values)
- **If MMS agrees with challenger, after reviewing actual data, it has two choices:**
  - **Apply to challenger only**
  - **Modify Average Exchange Differential for all affected parties**



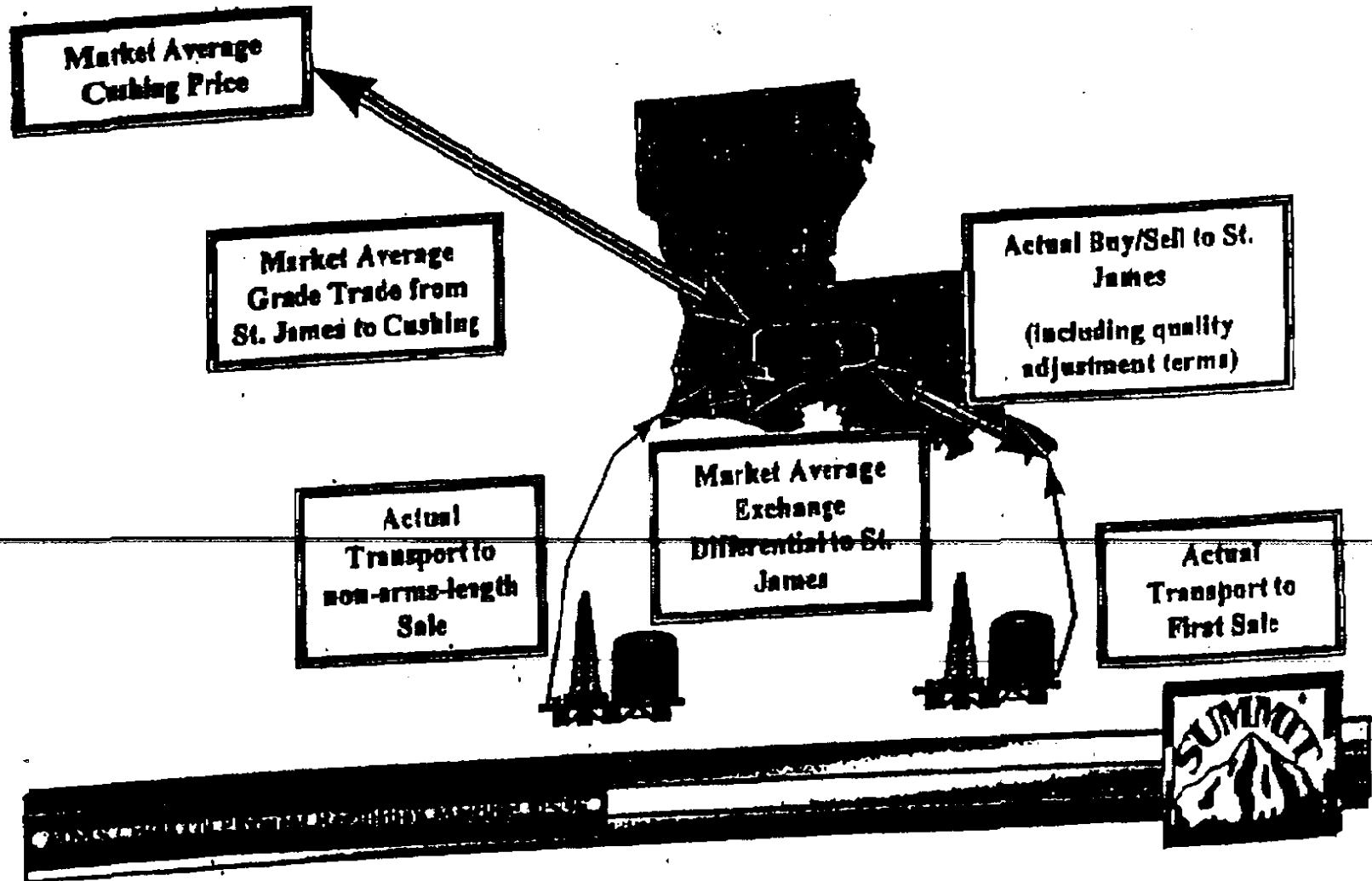
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# Use of Mean or Median for Average Exchange Differential

- Should be volume weighted calculation
- Use of the Mean should provide best approximation to total value which would have been received by MMS if all parties had paid on actual receipts.



# Conceptual Summary of Suggested Revised MMS Payment Regulations



# Attributes of New Suggested MMS Crude Oil Payment Regulations

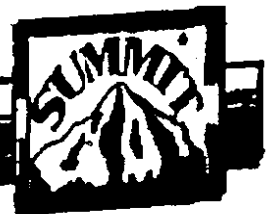
- Matches payment regulations to typical crude oil marketing practices
- Allows companies to continue paying on actual receipts where appropriate
- Market average price differentials could be used to establish "pseudo-postings" to fit into existing oil company payment systems with essentially no system modifications required

■ MMS CRUDE OIL PAYMENT REGULATIONS

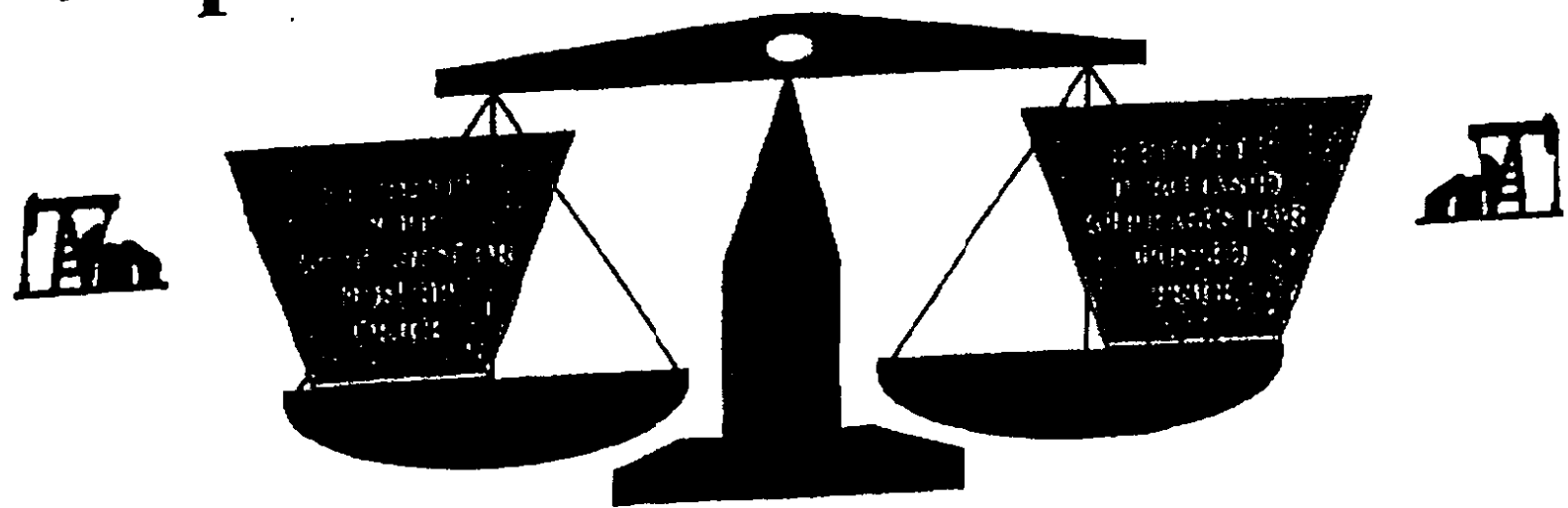


# Summary of Current Crude Oil Marketing Practices

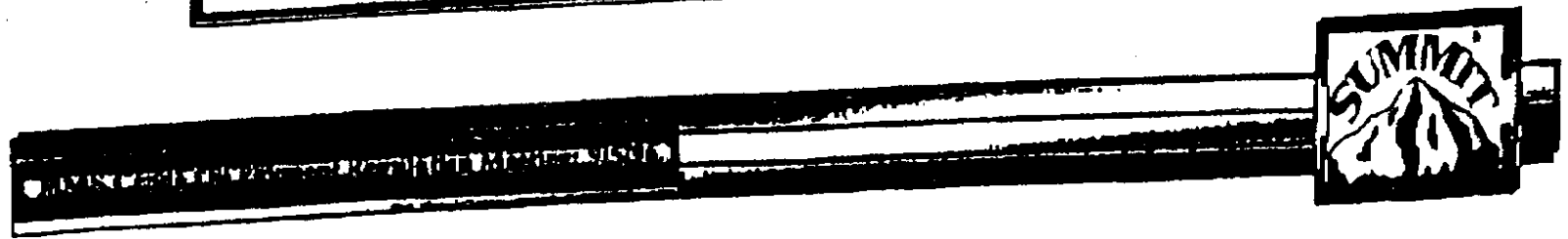
- Few truly outright sales by major producers
- Independents commonly sell outright
  - Many Independents use sophisticated sales
- Most Majors utilize buy/sell exchanges
- Overall Balance concept used by several Majors
- Price adjustments for quality are commonly negotiated on each contract



# ***“Overall Balance”: Implied Exchange Transaction***



As long as two companies sell approximately equal volumes to each other, the absolute price isn't important. In fact, because of reduced royalty and severance tax payments, the volumes don't even have to be exactly equal for both parties to benefit from setting the posted lease prices below full value. There may not even be written contracts reflecting the exchanges.



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Subject: Oil Royalty Rule Investigation  
From: bspeir@erols.com at Internet  
Date: 5/19/99 10:16 PM

Dear Senator Murkowski:

I am the former Department of Energy employee who, according to a Dow Jones news article today, was the subject of a letter signed by you and Senators Domenici and Nickles asking for an investigation of my involvement with the Project on Government Oversight. If my name sounds slightly familiar to you, it is because I performed the DOE's 1994 study the justified exporting Alaskan oil.

Below you will find a copy of an e-mail I sent to the Dow Jones reporter providing background on the timing and nature of my involvement with both the Project and royalty matters. As you can see, you have been getting (I believe) some bad info regarding the royalty rule business. Let me not mince words on that, however. The MMS is right in plugging the loopholes. You don't have to look at as many oil contracts as I have to see that.

You may wish to forward this to your letter's cosigners. If you wish to contact me directly, I am at 703-237-5420.

Robert A. Speir

#### ATTACHMENT

Subject:

Story on Royalty Rule

Date:

Wed, 19 May 1999 21:42:19 -0400

From:

"Robert A. Speir" <bspeir@erols.com>

Organization:

IIC

To:

campion.walsh@dowjones.com

Campion,

I am the former Dept of Energy employee referenced in your article on the royalty rule and the industry's attack thereon. Thanks for the balanced story. Carolyn Maloney is right, by the way, this is a convenient diversion by the industry and the congressional folks that have supported them.

As regards the Justice Department investigation, it seems that neither I

nor Bob Berman, the other person involved, can find out what that is about. No one has contacted me other than to alert me that I will be deposed in the larger matter of the government's fraud suit against these companies for royalty underpayment. That is a point that often gets lost in the industry's public comments. This issue is really about massive fraud by the companies. Amending the royalty valuation rule is about trying to see that they do not get away with it in the future.

As regards the royalty rule itself, Berman and I had little influence on

what the Interior Department is attempting to do to plug the loop holes industry wrote for itself in the current royalty payment rules during the Reagan Administration. All I did, in fact, was help the members of

the Task force you referenced see that the government was being cheated in California. We estimated that the underpayments and back interest due is between \$250 and about \$850 million. To date, Interior has not collected a cent.

The Task Force conclusions started the Minerals Management Service on the way to finding a set of rules that would eliminate the cheating. However, it was certainly not the work of two scheming bureaucrats. There were five primary members of the group: two from the royalty office in Denver, one attorney from the Solicitor's Office in Washington, one member from the Commerce Department and me. We also demanded and ultimately received support from the Minerals Management Service to conduct targeted audits of two large oil companies. The audit team's findings independently confirmed our own, which were drawn from review of court-sealed material from the State of California's suit

against the companies. I might add that Berman was NOT part of this process.

I don't think that many Interior Department reports received as much internal scrutiny as the Task Force report. The findings were debated, argued, and vetted over a four month period. Ultimately, they were accepted by Interior Department management through the Assistant Secretary for Land and Minerals. My involvement with Interior on this subject ceased with issuance of our final report in May of 1996.

At that time, the Project on Government Oversight-POGO- had not even considered joining the false claims suit that ultimately brought them a share of Mobil's \$48 million settlement. I initiated my retirement process in the summer of 1997, and retired in October 1997, about three days after I turned 55 and was first able to retire without penalty. The precipitating cause of my retirement was a \$25,000 buyout offer to employees in my office that was scheduled to expire on November 7. At that time there was no serious thought that any of the companies accused

of fraud by the Justice Department would settle. Mobil settled in the late summer/early fall of 1998 and POGO received money in September, I believe.

At that time, POGO notified the Justice Department (I believe through the U.S. Attorney's Office in Texas) of the intent to share its receipts

as a public service award with one former and one current government employee. The Justice Department took no action to attempt to block this action nor to encourage POGO to refrain from it.

As I noted above, both Berman and I are being deposed by the oil companies in the matter of the fraud suit. Less than a week before Berman was to be deposed, the Justice Department, on advice of the court

in Texas, notified the oil company defendants by letter that he had received money from POGO. They promptly leaked the letter to all their congressional supporters to whip up this issue. Shortly before the deposition, and long after the original notification by POGO, Berman's attorney sought out the ethics office at Justice and was informed that an investigation had been opened a short time before.

This note has gotten longer than I planned, so I will stop for now. At some point, and after I have cleared my additional comments with my attorney, you may want to talk to me further. Until then, I hope that this helps add a few facts to what otherwise has been a very one-sided story.

Robert A. Speir

Author: David Hubbard at "mms-denver-gh-4"  
Date: 9/18/96 10:34 AM  
Priority: Normal  
TO: Deborah Gibbs-Tschudy  
TO: Donald Sant at "MMS-DENVER-85-1"  
TO: James Shaw at "MMS-DENVER-85-1"  
TO: Peter Christnacht  
Subject: Oil Valuation

----- Message Contents -----

FYI; haven't yet heard from Commerce.

----- Forward Header -----

Author: "bob.speir" <bob.speir@hq.doe.gov> at "smtp"  
Date: 9/18/96 11:54 AM  
Subject: Oil Valuation

Dave,

I'M B--A--C--K! See attached note. I tried to call Sant but I could not get the number to ring. Will you please put me on the list as the DOZ commentator?

Bob Speir

P.S. Think about rewriting the regs to do away with any recognition of affiliate transfers. Define the lessee to be the parent corporation and all its consolidated and unconsolidated entities that it directly or indirectly controls (this definition is consistent with normal accounting practices). This makes the regs MUCH simpler.

----- Forward Header -----

Subject: Oil Valuation  
Author: Abe KASPEL at FO-03  
Date: 9/9/96 12:25 PM

Don Sant of MMS called and asked for our participation in reviewing their proposed oil valuation regulations. He is sending a letter and then we will name you. OK? Also, he asked if we knew someone at Commerce who knew about oil valuation. I said I'd ask you. I'm out for the rest of the week -- so could you please call Don at (303) 231-3889. Thanks. Abe

**Robert A. Speir**

**From:** Bob SPEIR (Bob SPEIR at po-03) on behalf of Bob SPEIR  
**Sent:** Friday, April 25, 1997 3:57 PM  
**To:** david\_hubbard@amtp.mms.gov  
**Subject:** IPAA Testimony

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regapex.wpd

Dave,

Our Management asked me to review IPAA testimony. Thought I would share this with you. In particular, look at 88 Oil's relationship to Basin. Don't you wonder if True Oil's affiliate sales to 88 get the same premium over posting that you would expect to see in Basin's sales to 88? Hint hint.